

Broad push against U.S. rules: Behind the scenes

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A stark objection from Canada's top banking regulator to a key plank in the overhaul of the U.S. banking system is just the public culmination of a flurry of behind-the-scenes discussions involving the Bank of Canada and the Department of Finance.

Sources say discussions took place shortly before Christmas when industry concerns about the Volcker Rule - a key component of the Dodd-Frank Wall Street Reform Act - were communicated to regulatory and government officials, including Mark Carney, the governor of the Bank of Canada.

The Volcker Rule is a highly controversial post-crisis reform aimed at limiting the trading banks can do on their own behalf and through relationships with hedge funds and private-equity groups. Critics say it will squeeze liquidity out of the Canadian bond market. Sweeping global compliance requirements created by what amounts to "extra-territorial" regulation are expected to drive up costs at Canadian banks.

This opposition touches on areas of concern for Canada's central bank, finance department and the Office of the Superintendent of Financial Institutions (OSFI), which oversees the safety and stability of the country's banks.

The discussions in December led to a cascade of letters to U.S. authorities, including the Department of the Treasury and the board of governors of the Federal Reserve System. A standout among them was a letter from OSFI Superintendent Julie Dickson, which warned that the Volcker Rule restrictions could undermine the financial condition and stability of banks outside the United States by interfering with crucial funding and market-making activities.

"OSFI is concerned that the draft regulations may have the unintended consequence of significantly impeding Canadian and other foreign financial institutions' ability to manage their risks in a cost-effective manner, which could give rise to prudential concerns in Canada and abroad," Ms. Dickson wrote in the letter.

Some industry sources expressed surprise that a prudential regulator such as OSFI would take the position in a public forum, rather than communicate it privately.

But **Terry Campbell**, president of the **Canadian Bankers Association**, said the industry group is pleased the regulator stepped up and hopes other senior officials will do the same.

"We have made our concerns known to ... federal Finance [representatives] and the Bank of Canada and we hope they share our concerns," Mr. Campbell said in an interview Thursday. "Our hope would be that other bodies of the federal government can make their concerns known to U.S. authorities, but that will be a decision they will have to make."

If the federal Finance Minister, Jim Flaherty, were to step up, it would not be the first time he has waded in on an issue involving the reach of the U.S. government. Last fall, Mr. Flaherty wrote a letter for publication in major U.S. newspapers in which he criticized a crackdown on tax evasion by the U.S. Internal Revenue Service, saying it had "far-reaching extraterritorial implications" and "would turn Canadian banks into extensions of the IRS."

With or without such political allies, Mr. Campbell said the Canadian Bankers Association will continue to press its case with government and regulatory authorities in both the U.S. and Canada.

In a preliminary letter of its own, the bankers' association said the extensive Volcker requirements could undermine the "competitiveness and efficiency" of Canada's financial institutions and markets and have "a significant and negative impact on the liquidity of Canadian government and corporate debt."

Sources say at least one of Canada's largest five banks will be represented when the U.S. House Financial Services Committee convenes later this month to debate the Volcker Rule.

The rule, which is intended to go into effect in July with a two-year phase-in period, has already drawn sharp criticism from U.S. banks that fear their profits will be crimped. International financial institutions are expected to voice objections similar to those expressed in Canada when the Institute of International Bankers submits a letter to U.S. authorities in the coming days.

There has already been some headway made, with U.S. market authorities agreed to extend an initial 90-day comment period through mid-February.

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